

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer

Natwar M. Gandhi
Chief Financial Officer



MEMORANDUM

TO: The Honorable Linda W. Cropp
Chairman, Council of the District of Columbia

FROM: Natwar M. Gandhi
Chief Financial Officer

DATE: July 7, 2003

SUBJECT: Fiscal Impact Statement: "District of Columbia Retail Incentive Act of 2003"

REFERENCE: Bill Number 15-306 as Introduced

Conclusion

Funds are not sufficient in the proposed FY 2004 through FY 2007 budget and financial plan to enact the "District of Columbia Retail Incentive Act of 2003". **This act would not have an impact on the FY 2004 budget, but could cost up to \$5.39 million in the period between FY 2004 and FY 2007.**

Background

The District of Columbia Retail Incentive Act of 2003 would change the rules of the current tax increment financing (TIF) program for certain retail projects. Under this legislation, the Mayor would designate places having difficulty attracting retail stores as Retail Priority Areas and would issue bonds to support new Retail Development Projects. Within each Retail Priority Area there would be a number of individual TIF Areas. Each TIF Area is essentially a footprint of a Retail Development Project – home furnishing or apparel business – that has been approved by the Mayor and a committee to include the Deputy Mayor for Planning and Economic Development and retail brokers and property owners appointed by the Mayor.

The proposed legislation establishes the Downtown Retail Priority Area as the first Retail Priority Area and sets a \$30 million limit on the amount of bonds that can be issued for that area.

The \$30 million allocation to the Downtown Retail Priority Area, in conjunction with other outstanding and pending TIF debt, would bring the District's outstanding TIF debt to \$178.9 million, or within \$121.1 million of the \$300 million cap.

Project	TIF Bonds
Gallery Place	\$73.5 million
Mandarin Oriental Hotel	\$46.0 million
Spy Museum	\$6.9 million (notes)
Capitol Hill Towers (Pending Council Approval)	\$11.5 million
Embassy Suites (Pending Council Approval)	\$11 million
<i>Downtown Retail Priority Area (Pending Council Approval)</i>	<i>\$30 million</i>
Total Outstanding TIF Bonds	\$178.9 million
Remainder of \$300 Million TIF Bond Cap	\$121.1 million

The Mayor also retains the authority to abolish any Retail Priority Area, as long as it will not adversely affect the security of the holders of the bonds.

This bill would establish rules of operation for Retail Priority Areas that differ from those for other TIF projects. A rating system would be created to evaluate potential projects based on such factors as the uniqueness of the retailer. A numeric formula would be established to produce a subsidy amount based upon a project's rating. The Mayor would establish a committee, which would be comprised of the Deputy Mayor, retail brokers and property owners in the Downtown Retail Priority Area. This committee would establish the aforementioned rating system and numeric formula for allocation of bond proceeds and would recommend potential TIF Areas. The Mayor would certify the amount of bond proceeds allocated to a particular project, certify the designation of each TIF Area and certify each project's eligibility to become a TIF Area. Every participating building owner must enter into a development agreement with the Mayor.

Bonds cannot be issued nor their proceeds disbursed until the TIF Area is open for business with the public. Once the business is open, the sales tax increment revenues generated by the TIF Area would be deposited into one or more separate tax increment allocation accounts within the General Fund. The sales tax increment is a dedicated revenue source that would be pooled and used to pay debt service on all of the individual TIF Areas within the Retail Priority Area. The majority of the sales tax increment would be used to pay for retail development costs; however, \$1 million may be used for administration of the program, and \$5 million may be used for streetscape and façade improvements.

Financial Plan Impact

Funds are not sufficient in the proposed FY 2004 through FY 2007 budget and financial plan to enact the "District of Columbia Retail Incentive Act of 2003". This act would not have an impact on the FY 2004 budget, but could cost up to \$5.39 million in the period between FY 2004 and FY 2007.

This estimate assumes the pooling of tax increment revenue from all TIF Areas within the Retail Priority Area and using the pooled money to make debt service payments on all outstanding debt. With this arrangement, the successful retail projects support the unsuccessful retail projects. Under the regular TIF process, successful TIF projects would return excess tax increment revenue to the General Fund. Under the proposed alternative structure, excess tax increment revenue generated by successful businesses would be used to cover debt service for unsuccessful businesses rather than reverting into the General Fund.

The proposed structure uses variable rate notes and bonds. An increase in the interest rate of the bonds would increase costs for both the businesses and the District. The increased costs for businesses would increase the businesses' failure rate. For example, at the end of June 2003, the London Interbank Offered Rate (LIBOR) plus 325 basis points would be approximately 4.75%. If the average LIBOR for the past eight years were used, the interest rate would be 8.25%. A 3.5% interest rate change is significant enough to cause many businesses to fail to meet debt service.

The impact of this bill was determined by assuming that by FY 2005 half of the retail businesses would fail and that the District would be required to pay half the yearly debt service. The assumption was made that \$10 million in TIF bonds would be sold per year in FY 2004 through FY 2006. In FY 2007, the legislative cap would have been met and debt service would be paid on the \$30 million. We also assumed that the interest rate would be variable, starting at LIBOR plus 325 basis points and increasing by one hundred basis points a year. The chart below shows the District's liability if half of the retail establishments fail.

Estimated Cost to the Financial Plan					
(\$ in millions)					
	FY 2004	FY 2005	FY 2006	FY 2007	4-Yr Total
Debt Service	\$0.00	\$0.86	\$1.78	\$2.76	\$5.39